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No. 885

Supreme Court of the United States

October Term, 1944.

A. M. ANDERSON, Receiver of the National Bank of Kentucky of Louisville, - - Petitioner,

versus

R. C. TWAY, - - - - - - - Respondent.

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SIXTH CIRCUIT.

BRIEF IN SUPPORT OF PETITION.

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IN THE

Supreme Court of the United States

October Term 1944.

No. _____.

A. M. ANDERSON, RECEIVER OF THE NATIONAL BANK OF KENTUCKY OF LOUISVILLE, - *Petitioner,*

v.

R. C. TWAY, - - - - - - - - - *Respondent.*

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SIXTH CIRCUIT.

To the Honorable Chief Justice and Associate Justices of the Supreme Court of the United States:

A. M. Anderson, Receiver of the National Bank of Kentucky of Louisville prays that a writ of certiorari issue to review the judgment entered June 12, 1944 (R. 1355), and the Order denying the petition for rehearing entered September 11, 1944 (R. 1463), in the United States Circuit Court of Appeals for the Sixth Circuit, in Cause No. 9250 on the docket of said Court. Said judgment affirmed, by divided vote, the judgment of the District Court of the United States for the Western District of Kentucky finding in favor of respondent and overruling the motions of petitioner for judgment and for a new trial.

OPINIONS BELOW.

The memorandum of Judge Taylor, in the District Court, is not reported, but appears in the record (R. 1296). The opinion of the Court of Appeals is unusual, in that it is the dissenting opinion of Judge Simons, with a limited and partial concurrence by Judges McAllister and Hicks and is reported in 143 Fed. 2d 95 (R. 1359).

JURISDICTION.

The judgment of the Circuit Court of Appeals was entered on June 12, 1944 (R. 1355). The petition for rehearing was denied on September 11, 1944 (R. 1463). On December 4, 1944, this Court extended the time for filing this petition for certiorari to January 31, 1945.

The jurisdiction of this Court is invoked under Section 240(a) of the Judicial Code, as amended by the Act of February 13, 1925, 28 U. S. C., 347.

QUESTIONS PRESENTED.

1. The first question concerns the fundamental right of cross-examination inherent in due process, which was entirely denied the petitioner in the trial before a jury in the Court below, under the following circumstances:

Defendant (Tway) borrowed money from the National Bank of Kentucky and gave his note to the Bank. The purpose of the loan was to pay his subscription for BancoKentucky stock. Sued on the note by Receiver, his defense was that the Bank falsely represented the condition of the Bank and the purpose of BancoKentucky. Defendant did not call any witnesses as to the alleged falsity. He relied exclusively on reading to the jury excerpts from unsworn papers, to-wit: (a) National Bank Examiners' reports, containing hearsay and secondhand information, the accuracy of which the Examiner said he could not guarantee; (b) A Bill in Equity, filed by Receiver claiming damage for dereliction of duty against the Bank's directors; (c) A table of earnings prepared by an accountant employed by the Receiver in another case.

The District Court overruled all objections of petitioner and permitted counsel for defendant to read to the jury such unsworn documents without calling as witnesses the persons responsible therefor. The Receiver was thereby denied all opportunity for cross-examination as to the competency, truth and accuracy of the hearsay and other statements made in such documents.

The question presented is whether, in a jury trial, the admission of such documents constitute a departure from the accepted and usual course of judicial proceedings and denies the party accused of fraud his constitutional right of cross-examination and due process of law?

2. Is hearsay evidence legitimatized and made legal proof by being included in an official report?

3. After the unverified Bill in Equity against the Bank directors was read to the jury, petitioner offered in evidence the final opinions and decrees of the Court in the Directors' Liability case, wherein the Court found that certain material allegations of the Receiver's Bill in Equity, read by plaintiff to the jury, were not proved, but the Trial Judge excluded said opinions and decrees from the consideration of the jury.

Did the Trial Judge, in refusing to permit the petitioner to show that the courts had not sustained said allegations of said unverified Bill in Equity, and by such refusal making the allegations of said Bill unimpeachable proof of the truth thereof, depart from the accepted and usual course of judicial proceedings and deny the petitioner due process of law?

4. After the trial, new evidence was discovered, which the Court of Appeals described as showing that the defendant made "concededly false representations to the Receiver" and gave "concededly untrue evidence in the trial below" (R. 1371). Petitioner moved for a new trial, in order to present said evidence to the jury, which the Court denied.

Did the Court, in refusing to reopen the case in order to permit a jury to pass upon such evidence and the effect thereof on the credibility of the defendant (who was the sole witness on the material factors in the case) depart from the accepted and usual course of judicial proceedings and deny to the petitioner his right to a jury trial on the true facts?

5. The trial Court charged the jury that even if defendant in buying Banco stock participated with the Bank in *ultra vires* acts, that fact was "immaterial" (R. 1216) and not to be considered by the jury. Was the charge of the Court contrary to applicable decisions of this Court, particularly, where defendant admitted that he knew that the Bank in selling such stock was acting beyond its corporate powers?

6. Where stock acquired with money borrowed from the National Bank is retained by defendant, together with dividends thereon and said stock had both a considerable market value and intrinsic value at the time of its purchase and at all times prior to the failure of the Bank and thereafter the value which it had at the time of purchase was lost, due to independent acts of the corporation after defendant became a stockholder thereof, should petitioner be charged with said loss of value due to the independent acts of the corporation arising subsequent to defendant's acquisition of his stock therein?

SUMMARY STATEMENT AS TO QUESTIONS 1, 2 AND 3.

Officers and directors of National Bank of Kentucky caused BancoKentucky Company, a Delaware corporation, to be organized. They solicited subscriptions to its stock. Defendant, Tway, was urged by Thieman, a Bank Vice President, to buy stock. "Tway was a big operator—his monthly stock investments carried in his own name, averaging $218,000.00 in 1922, $473,000.00 in 1923, and his overdrafts with the Sales Company for that purpose reaching $461,000.00 in 1930" (R. 1370).

Tway subscribed for 2,000 shares of Banco stock at the issue price of $25.00 per share (R. 169). On October 1, 1929, he borrowed $50,000.00 from the Bank for the purpose of paying for his subscription. At the same time he gave a note, due in four months, to repay this loan (R. 130). He agreed to pledge the Banco stock as collateral security for the payment of the note (R. 84, 85). The loan was credited to Tway's personal checking and deposit account (Ex. 9, R. 86). Tway then drew his check, payable to the BancoKentucky Company, for $50,000.00 (Ex. 10, R. 88). The 2,000 shares of Banco stock were issued in the name of R. C. Tway by the Louisville Trust Company and pursuant to Tway's power of attorney were delivered to the Bank and held by the Bank as collateral to Tway's note.

Tway received the regularly quarterly dividends paid by Banco on his stock (Exs. 20, 21, 22, 23, R. 113). He renewed his note as it became due and paid

the interest accrued thereon (R. 89, 79). This continued until the close of the Bank.

After the Bank closed, Tway continued to pay interest on his note (R. 82, Ex. 1, R. 78). He also filed his affidavit with the Receiver, for the purpose of securing an offset of his deposit account and other deposit accounts, including the R. C. Tway Special Account. He swore that he owned these accounts (R. 134, 135). In this affidavit, Tway further acknowledged his indebtedness to the Bank on the note. On the faith of this affidavit, the Receiver granted Tway the offset. Tway also made a payment on account of principal, which, together with the offset, reduced the balance due on the note to $45,000.00 (Ex. 1, R. 78).

Numerous similar notes had been given to the Bank, promising to repay money borrowed for the purpose of acquiring Banco stock. At the outset, said notes aggregated approximately $4,000,000.00, but the total was materially reduced by payments thereon. When notes were not paid, the Receiver sought to enforce collection by suit. One of these suits was instituted against Dant, who asserted in his answer as a defense to his note liability that the Bank had defrauded him by misrepresenting its condition and the purposes for which BancoKentucky was formed. Other defendants copied Dant's defense on a duplicating or ditto machine, so that it became known as a "ditto defense" (R. 455, 465, 466). The present suit was brought against Tway to recover the balance due and unpaid on his note. He thereupon copied into his answer, with-

out change, the language of the Dant defense. The Tway case was the first case tried. Twenty other cases were continued, pending a determination of the law in the Tway case. Thus the present case is a type case upon the outcome of which a large number of pending suits aggregating $640,000.00 await.

The suit of the Receiver against Tway was a common-law action to recover money only on his promissory note and was tried before a jury. Tway was the sole witness as to the alleged misrepresentations. He testified that he relied exclusively on the representations of Thieman, a Bank Vice President (R. 127). Tway exonerated Thieman of any intent to misrepresent (R. 127, 348, 352). Thieman's good faith was admitted to be beyond question, since he had invested his personal and his family's fortune in Banco stock, in the firm belief that his statements to Tway, concerning said Company, were true (R. 352, 657).

The alleged misrepresentations were:

1. That the National Bank of Kentucky, to be acquired by Banco, was in good condition, whereas in fact its assets included slow, doubtful and criticised items.

2. That Banco's purposes were correctly shown in the Prospectus, whereas in truth the purpose was to acquire from the Bank its bad assets.

Tway testified to the making of the representations, but not to the falsity thereof. On the contrary, he said that he assumed the representations to be true. No

witness was called to testify to the alleged falsity of said representations. Instead of calling any witnesses, Tway's counsel, over the objection of petitioner, was permitted to introduce in evidence and read to the jury a large number of excerpts from certain unsworn and unverified papers, to-wit:

1. Counsel read to the jury reports of National Bank Examiners to the Comptroller of the Currency, copies of which were sent to the Bank. These reports contained a vast quantity of hearsay information for the truth of which the Examiner expressly disclaimed any responsibility in the following language:

> "Much of the information in regard to the assets of the Bank is of such a character as to make it necessary for the Examiner to rely upon the good faith and assurances of his informants, and while the Examiner regards the statements so accepted by him as correct, he is, necessarily, not in a position to guarantee the accuracy of such part of the information as may not have been obtained at firsthand."

2. Counsel also read to the jury the voluminous Bill in Equity, filed by counsel for Receiver's predecessor against Bank Directors to recover damages for alleged negligence and statutory violations. This unverified Bill, after extensive hearings, was judicially held not proved in certain material particulars, which were, nevertheless, read to the jury and the Receiver was not permitted to show by the final judgment and

opinions of the Court that the facts alleged in the Bill and read to the jury had been disproved.

3. A tabulation of earnings, prepared by an accountant employed by Receiver for use in another case.

Conceding that the papers read to the jury were authentic copies of the originals, the Receiver objected to this extraordinary and unusual method of proof, for the obvious reason that the Bank Examiners, who prepared the reports to the Comptroller of the Currency, were not called as witnesses and placed under oath and thus made available for cross-examination, and because said reports were replete with hearsay, speculation, and secondhand information, to which the Examiner could not have testified had he been on the witness stand. Cross-examination is a fundamental right, even where it would be merely exploratory. In the present case, it was of paramount importance, in order to enable the jury to separate the parts of the reports based on the Examiner's personal examination of the books of the Bank from pure hearsay, for the source and accuracy of which the Examiner disclaimed responsibility. On the vital issue of whether the true purpose of Banco was to remove bad assets from the Bank or to engage in group or investment banking, as set forth in the Prospectus, the only evidence was the following hearsay statement contained in the Bank Examiner's report:

> "Your Examiner was advised that a plan is in contemplation, whereby a sort of finance and holding company will be organized with a large capital

> stock, say $20,000,000.00. The holding Company will hold, among other things, the stock of the National Bank of Kentucky and its affiliated bank through a surrender and exchange of the stock of the Bank for stock of the Company on some satisfactory basis. *It is also contemplated that the holding company will acquire, and through a term of years work out certain assets of the Bank, among others, probably Kentucky Wagon Manufacturing Company.*"

No other evidence was introduced to support the claim that the true purpose of Banco was to take over bad assets, such as the Kentucky Wagon Manufacturing Company.* The Court charged the jury:

> "Now the *only* evidence—at least of witnesses —tending to establish that is perhaps an *observation* in the Bank Examiners' reports, which is before you for consideration, that one of the officers, *presumably* Brown, had on *one occasion* stated that a corporation would be organized for *that purpose.*" (R. 1216.)

The Court will note that the Examiner does not say who advised him, and the Court's statement to the jury that it was an officer "presumably Brown" is a purely speculative assumption, emphasizing the danger of admitting hearsay evidence, not under oath and not subject to cross-examination.

Under the Federal Rules, the Receiver could not have called the Examiners for *cross*-examination. Thus

*This was one of the most severely criticized assets of the Bank, in which the ultimate loss exceeded $2,000,000.00. Atherton v. Anderson, 86 Fed. 2d 518; 99 Fed. 2d 883.

the right of cross-examination inherent in due process of law was effectually denied the Receiver. When the Receiver objected, the Court, although expressing "serious doubt" (R. 550) admitted the Examiners' reports *"in toto,"* including *all of the hearsay, speculative* and *second-hand statements contained therein.* In so doing, he stated:

> "The Court: Over my own opinion and idea and controlled by what appears to be the modern trend, I shall permit the jury to consider the Examiners' reports *in toto,* but shall advise the jury that *there was no opportunity for cross-examination of the Examiners."* (R. 1202.)

Counsel for petitioner made timely objection and moved to withdraw a juror and continue the case because of the prejudice resulting from this ruling (R. 238), and further stated (R. 1203):

> "This being our first opportunity to raise the question because it is the first time the matter has been finally ruled upon, we wish not only to object and except to that ruling[1] * * * but to raise the question that the ruling denies the plaintiff in this case its constitutional right under the Federal Constitution, viz.: the right to be confronted with the witness and cross-examine him, and the right to have the oath administered to the witness, and the right to have the testimony given in open court, and this ruling permits documents that contain conclusions, all kinds of hearsay by witnesses not shown to be qualified."

[1]Admitting the Examiner's reports *"in toto."*

The Court stated that he was "disposed to agree with counsel, not necessarily on his question as to the substantive rights, but *on the danger of the relaxation of the hearsay rules of evidence,*" but, nevertheless, adhered to his ruling (R. 1203).

The Court permitted the jury to find a verdict based upon these reports although the jury was cautioned:

> "That in some instances obviously the opinion expressed by the Examiner was based on matters *outside* the records of the Bank and were *opinions* formed upon facts not disclosed because the Examiners were not present and were *not available for cross-examination* by counsel representing the Receiver" (R. 1218).

The jury was also told that they were the exclusive judges of the facts and were at liberty to disregard the comments of the Court thereon (R. 1211).

The Receiver further objected to the defendant reading to the jury excerpts from the long Equity Bill filed by counsel for Receiver's predecessor, seeking to recover damages from the Bank Directors for alleged negligence and statutory violations, because it was an unverified pleading between different parties on different issues and in addition because the material allegations relied on in the present case as proof of the facts alleged had been judicially found to be incorrect upon the trial of the issues raised in the case against the directors (Atherton v. Anderson, 86 Fed. 2d 518, 99 Fed. 2d 883).

The trial Court overruled these objections and also excluded from evidence the proffer made by the Re-

ceiver of the opinions, and final judgment of the Court holding that these allegations of the Equity Bill had been disproved. The effect of this ruling was to make the statements contained in these unverified documents unimpeachable evidence and conclusive of the facts stated therein. The following is an excerpt from the record. Counsel for petitioner said (R. 1095):

> "We would like to offer the opinion of Judge Tuttle on illegal dividends; Judge Simons' opinion on losses on Banco stock, and Judge Hicks' opinion on losses on Banco stock *and the final entry.**
>
> "By the Court: I have concluded that they are inadmissible and we will not receive them in evidence. They may be proffered and made a part of the record" (R. 1172).

Counsel for petitioner then stated:

> "If the Court please, I have *the final decree in the Directors' case* and that is in a different category than the opinions in the other cases. It merely shows what the final decree held in that case."

Counsel for defendant objected, and the Court *refused* to submit the same to the jury (R. 1172, 1173).

We also objected to reading in the evidence excerpts from a report made by an accountant (White) employed by the Receiver in another case, because he was not called as a witness and not made available for cross-examination. Further, the correctness of the schedule of this accountant had been challenged by cross-exami-

*Opinions are part of record in Cause No. 7298, U. S. C. C. A. 6th and were ordered considered a part of this record on appeal.

nation in the case where it was offered in evidence and had been contradicted by a schedule prepared by other accountants (Vol. 2, R. 676, 677, 678, 684). The Court overruled the objection and counsel for defendant objected "on the ground that the witness who made the report is not here and we have no opportunity for cross-examination" (R. 677, 678).

The above papers which were read to the jury *constituted the only evidence of the alleged fraud.* Thus the Bank was convicted of fraud (1) without any witness being called to the stand, (2) without any sworn testimony and (3) without having the right to either cross-examine or (4) to contradict or impeach the unverified allegations of the Bill in Equity. Further, the finding of fraud necessarily rests on hearsay statements, contained in the Examiner's Reports, which would not have been admissible from the lips of the Examiner had he been sworn and placed on the witness stand.

SUMMARY STATEMENT AS TO QUESTION 4.

In the course of the trial before the jury, Tway testified that he was the exclusive owner of the 2,000 shares of Banco stock from the time of his original purchase thereof to the date of trial (R. 306). After the conclusion of the trial, the petitioner discovered that two months after the purchase of the Banco stock by Tway, he had sold or transferred the same to the R. C. Tway Coal Sales Company, a corporation of which Tway was the principal, but not the sole stockholder (Ex. 3, following R. 1294). Thereafter the Coal Company and

not Tway was in fact the sole owner of the Banco stock. Liability for the purchase price of the stock became that of the corporation and Tway sustained no damages as a result of his purchase. Under these facts Tway, having sustained no damage, could claim no damages by way of defense.

Affidavits were filed on behalf of the petitioner, substantiated by records of the corporation, showing the sale of the Banco stock to the R. C. Tway Coal Sales Company (Ex. 3, following R. 1294). Tway made an affidavit, in which he admitted that the stock was owned exclusively by the corporation and not by him, as he had testified before the jury (R. 1283). In the affidavit he contended that he had acted as an undisclosed agent for the corporation in making the original purchase. The Receiver filed counter-affidavits tending to disprove the claim that Tway acted as an undisclosed agent and showing that he had purchased the stock and then sold it to the corporation (R. 1271, 1282). The Court of Appeals said that the newly discovered facts established that Tway made "concededly false representations to the Receiver" in the affidavit for offset and gave "concededly untrue evidence in the trial below."

The Court of Appeals points out that all of the material factors upon which Tway's defense rests were "supported only by the assertions of Tway himself and the jury's verdict may be explained only by its acceptance of Tway as a witness whose credibility and accuracy of memory could be relied upon." Judge Simons, in his opinion, then recites the judicial history of Tway's operations in stocks and concludes "in the

light of that history, which I am unable to ignore, and which the Court should not ignore, Tway's explanation of his concededly false representations to the Receiver and his concededly untrue evidence in the trial below is wholly incredible and might well be thought so by a *jury*. Since his claim of reliance upon fraudulent concealment in ignorance of the infirmities in the Bank's position, notwithstanding published criticisms of it which came to his notice prior to his renewals, payment of interest, and acceptance of dividends, rest entirely upon his own word a *jury* should be permitted to appraise the accuracy of his memory and the credibility of his evidence bearing upon the vital issues of the case in the light of the newly discovered facts. I think the Court should have granted the motion for a new trial."

Judges McAllister and Hicks were of the opinion that "newly discovered evidence which tends merely to affect the weight and credibility of evidence does not constitute a proper basis for a new trial. Under the circumstances of this case, it does not appear to me the denial of the motion for a new trial on the ground of newly discovered evidence that would *only affect the credibility of Tway,* was an abuse of discretion on the part of the district court." Thus the question arises: —Where the *sole* witness has given *false evidence* before a *jury* and the *verdict rests on such false evidence,* does the usual and accepted course of judicial procedure require a new trial, in order that the rightful triers of the fact, to-wit: the jury, may pass upon the credibility of the witness or may the Court take away the right to have a jury pass thereon?

SUMMARY STATEMENT AS TO QUESTION 5.

The National Bank of Kentucky promoted the organization of the BancoKentucky Company as fully set forth in the opinion of this Court in Anderson, Receiver, v. Abbott, 321 U. S. 349. Tway's case was based on the claim that the Bank was engaged in selling to him common stock of the BancoKentucky Company. In the opinion below, Judge Simons correctly said "It is agreed that the promotion of Banco was beyond the legitimate powers of the Bank and *ultra vires.*" Citing Dietrick v. Greaney, 309 U. S. 190; D'Oench, Duhme Co. v. F. D. I. C., 315 U. S. 447; F. D. I. C. v. Vest, 122 Fed. 2d 765 (C. C. A. 6).

In addition, this Court said in First National Bank of Ottawa v. Converse (1906), 200 U. S. 425, "A national bank has no power to engage in or promote a speculative business."

The loan of money by the Bank to Tway and the giving of his note to repay the loan were clearly proper banking functions. Tway asserts, however, that the purpose of the loan was to induce him to buy Banco stock. The promotion of Banco, the sale of its stock and any representations in connection therewith were all beyond the proper powers of a national bank. Tway's defense, based upon such *ultra vires* acts, was identical with the defense attempted in the D'Oench, and Dietrick cases, *supra.* In both cases, this Court held because of the "evil tendency of the acts to contravene the policy governing banking transactions" the

defendant was estopped to plead such acts to escape payment of his note.

The Court below said: "Here it is but claimed that Tway participated in a transaction which through experience he knew to be was beyond the authority of the Bank." In addition to knowing "through experience" he was specifically told by Thieman that the Bank was promoting Banco to "do and perform functions that a national bank could not do; that it could underwrite issues, invest—buy and sell stocks, underwrite mortgages, participate in management of industry and do a general business that could make a great deal of money" (R. 165). To the same effect, see R. 341, 345.

The Court below said that Tway "denied such knowledge and the question was one for the jury." It is apparent from the above record references that Tway did not deny knowledge that the enterprise was beyond the corporate powers of the Bank, but in any event the trial Court did not submit the question to the jury as Judge Simons indicated should have been done. On the contrary, the trial judge eliminated as a defense petitioner's claim that Tway participated and joined with the Bank in the promotion of BancoKentucky with full knowledge that he was participating in the *ultra vires* transaction. The trial Court instructed the jury that this was "immaterial" (R. 1216). This instruction, affirmed below, is contrary to the applicable decisions of this Court.

SUMMARY STATEMENT AS TO QUESTION 6.

At the time of the representations and the purchase of Banco stock (October 1, 1929) the issue price was $25.00 per share. The stock was listed on the Chicago Stock Exchange and regularly traded in at daily quoted market prices (R. 297). The market price appreciated so that on October 15, 1929, the market price of Banco was $34¼ per share, and Tway could have sold at a profit of approximately $18,000.00 (R. 294, 295). The disastrous stock market panic followed thereafter but notwithstanding the sensational collapse of all stock prices, the market price of Banco stock was such that Tway could have sold his stock for the cost price or at a slight profit (R. 301). Tway held for higher prices. The stock had a substantial market value until after the failure of the National Bank of Kentucky when it was quoted as low as $1.00 per share (R. 304).

Irrespective of market value, BancoKentucky stock had a substantial intrinsic value at the time of its purchase and for a long period thereafter. The only criticism of Banco assets made at the trial was with respect to the value of the stock of the Bank of Kentucky held by Banco. However, Banco also held the stock of The Louisville Trust Company and a number of other banks. The soundness of these institutions was admitted (R. 20, 379, 810). They constituted approximately half of the asset value of Banco stock.

The ultimate loss of all value of Banco stock was due to the independent acts of the directors of Banco. These independent acts consisted of a loan of $2,000,-

000.00 to James Brown made November 14, 1929 (R. 1038). The sale of the Brighton Bank in Cincinnati for a loss of $3,445,000.00 in the Fall of 1930, and a loss of $3,573,000.00 on the sale of the Pearl Market Bank at approximately the same time (R. 1060). Tway knew of these investments when they were made (R. 353-357). Further, the ultimate collapse was caused by the Caldwell deal made May, 1930, more than six months after Tway bought his stock (R. 777).

Tway was permitted, at the trial, to show these subsequent events as proof of damages and fraud. Judge Simons holds this was error since "neither Thieman nor the Bank was a guarantor of the financial success of the Banco venture and neither could be charged with knowledge of future events."

This Court said in Anderson v. Abbott "*The stockholders of Banco cannot escape responsibility for the inadequacy of Banco's resources merely because the choice of its investments was made by the officers and directors—acts in which the stockholders did not participate and of which perhaps they had no actual knowledge.*"

The defendant chose to retain the ownership of Banco stock. He received and kept the dividends thereon. It was not until suit on his note by the Receiver that he disclaimed liability. His defense is based solely on misrepresentations of the Bank, causing him damage *at the time of the purchase of his stock*. There is no reason why the universal rule that damages are the difference "between the price paid and the real intrinsic value of such shares at the time of their pur-

chase" should not have been applied. Hindman v. First National Bank, 112 Fed. 931 (1902). Opinion by Judge Lurton, subsequently a Justice of this Court.

In Smith v. Bolles, 132 U. S. 125, this Court said, "If the stock had a value in fact, that would necessarily be applied in reduction of the damages."

Instead of applying the settled law to the present case and instructing the jury to ascertain the damages sustained by Tway as the result of the alleged misrepresentations and to deduct the same from the amount due on his note, the trial judge instructed the jury that if there were any false representations, they should completely exonerate Tway from any liability on his note.

The net effect of the affirmance of these instructions has been to charge the Receiver with the losses in value which occurred long after the misrepresentations complained of and which were due entirely to the independent acts of the Corporation long after Tway became a stockholder thereof. Such rule is contrary to the opinion of this Court that "the stockholders of Banco cannot escape responsibility for the inadequacy of Banco's resources merely because the choice of its investments was made by the officers and directors." Tway's remedy with respect to improper investments was by action against the officers and directors of Banco for mismanagement.

REASONS RELIED ON FOR ALLOWANCE OF WRIT.

(Relating to Questions 1, 2 and 3.)

The Court of Appeals sanctioned such a departure, by the lower court, from the accepted and usual course of judicial proceedings as to call for the exercise of this Court's power of supervision. The departure, complained of, is that the lower court disregarded the requirements of the Federal Constitution with respect to due process of law and found the Bank guilty of a charge of fraud without any sworn evidence of the fraud and without the Bank having the right to cross-examine witnesses against it.

The Court further departed from the accepted and usual course of judicial proceedings by admitting as evidence of fraud hearsay statements contained in unverified documents and sustaining a finding of fraud based thereon.

The questions involved in the Tway Case herein presented will also arise in numerous cases now pending on notes given to the Bank by debtors who assert similar defenses. Twenty other cases have been continued awaiting the outcome of the present case. The amount involved ($640,000.00) is sufficient to be of importance to the large number of depositors of the Bank (30,906). However, the questions herein involved transcend in importance the immediate controversy between the Bank and its debtors. These questions involve the extent to which official documents and reports may be used in the trial of actions in the Federal courts to accomplish the introduction into evidence of hearsay

statements, opinions, speculation and assumptions of Federal officials and examiners, based upon second-hand information without the necessity of placing the author of such documents and reports under oath, and subjecting the person responsible therefor to cross-examination.

This is an important question of Federal law which has not been, but should be, settled by this court. The rule sanctioned below has far-reaching consequences—not confined to the parties to this case. It extends far beyond the supervision of national banks.

The trial court admitted the Examiner's reports "*in toto,*" including all of the hearsay statements, opinions and conclusions based upon second-hand information derived from undisclosed sources, *on the theory that said reports were official documents and were admissible under an exception to the hearsay rule.* This exception applies only to official reports and books recording primary facts, 20, Am. Jur. 866, Par. 1027. "Expressions of opinion and the making of conclusions, are not admissible in evidence as public records." The trial Judge recognized that the extension of the exception to the rule, which he permitted in the present case, was not only contrary to his personal opinion, but constituted a *dangerous* relaxation of the hearsay rules of evidence (R. 1203).

In the opinion of the Court of Appeals, Judge Simons said:

> "So with hearsay statements in the examiners' reports. While as official records they may be admissible to show such facts as are within the per-

sonal knowledge of the examiner, I doubt their admissibility in respect to statements clearly indicated as those of informants, whose accuracy is not guaranteed. Nagle v. United States, 145 Fed. 302, C. C. A-2.

"If such statements are admissible, then the faintest breath of rumor or scandal may be legitimatized as evidence merely by including it in an official report. This cannot be the law."

The separate opinion of Judge McAllister, in which Judge Hicks concurred, is silent on this subject.

Although Judge Simons says "This cannot be the law," it will not only become the law in the present case, but constitute a precedent for all pending and future cases, unless this court exercises its supervisory jurisdiction with respect thereto. Thus, the problem presented becomes one of vast importance because of the centralization of Governmental functions and the tremendous growth of official records and reports of various Governmental agencies and the numerous examiners employed by them, of which the court may take judicial knowledge.

If the inclusion of hearsay, the expression of opinions and conclusions based on unknown sources, and second-hand information may be introduced in evidence in support of charges of fraud, or as affirmative proof in any of the numerous issues which arise between citizens, or between citizens and their government, without the necessity of an oath or cross-examination merely because included in an official report, then our traditional conception of due process of law must be materially altered.

This Court has held that:

> "Cross-examination is a matter of right * * * It is the essence of a fair trial that reasonable latitude be given the cross-examiner even though he is unable to state to the Court what facts a reasonable cross-examination might develop. Prejudice ensues from a denial of the opportunity to place the witness in his proper setting and put the weight of his testimony and his credibility to a test, without which the jury cannot fairly appraise them. * * * In this respect a summary denial of the right of cross-examination is distinguishable from the erroneous admission of harmless testimony." Alford v. United States, 282 U. S. 687 (1931), at page 691.

See also the Ottawa case, 70 U. S. 268 (1865), at page 271.

Nor could the Bank call the Examiners as witnesses on its own behalf and at the same time cross-examine and contradict them. The Phil & Trenton v. Stimpson, 39 U. S. (14 Pet.) 448 (1840).

The action of the trial Court in permitting these unverified documents to go into evidence "*in toto*" was contrary to the applicable decisions of this Court safeguarding the right of cross-examination.

The decision of the trial Court permitting defendant to put in evidence the unverified equity bill of the Receiver, claiming damages against the directors, was contrary to the decision of this Court in Delaware County Commissioner v. Diebold Safe and Lock Co., 133 U. S. 473 (1890). The Court of Appeals recognized

that this was so and also that it was contrary to the accepted practice in Kentucky (Rankin v. Maxwell, 9 Ky. 828). However, the Court of Appeals disregarded the opinion in this Court in favor of the so-called "modern view," citing The Rockland v. Farnsworth, 89 Me. 481 (1897). But the trial Court went beyond the mere admission of this unverified pleading as affirmative proof of fraud. The trial Court held that the allegations of the Bill could not be impeached or contradicted by showing that upon the trial and decision of the Directors' case many of the material allegations relied on by the defendant had not been sustained. The Receiver offered in evidence the opinions and the final decree of the Court holding that certain of these material allegations read to the jury were not proved. The jury was charged that they could consider the allegations of the Bill in Equity as proof, but were prevented from knowing that such allegations had been judicially disproved. Although the Receiver recovered damages against the directors on certain items of his claim, he was denied recovery on the particular allegations relied on by defendant in the present case. For example: The Receiver contended in the Equity Bill that the directors were liable for loans made on Banco stock on the theory that the Bank and Banco were in effect a single entity. The Court held against this claim. Atherton v. Anderson, 86 Fed. 2d 518, at page 536 (C. C. A. 6, 1936).

Although Judge Simons said in the opinion in the present case that the Equity Bill was properly admitted, he also said that:

> "The party who made the pleadings is, however, permitted to show that his allegations were erroneous. (Citing cases.) Since the opinion in Atherton v. Anderson, *supra,* was an adjudication that there was no fraudulent intent in the organization of Banco, the Receiver should have been permitted, by means of it, to demonstrate the error in the allegations of his pleading."

The majority Judges said nothing with respect to this fundamental error.

Although counsel for Tway, in the Court of Appeals, said he did not now rely on his allegation that Banco was organized for the purpose of removing bad assets from the Bank, Judge Simons correctly said:

> "That issue was, however, submitted to the jury and there can be no doubt that the evidence bearing thereon was prejudicial."

Again the majority Judges are silent. We submit that the action of the trial Court in receiving in evidence an unverified Bill in Equity, which Professor Wigmore characterizes as "conventional rigamarole" and for this reason not receivable in another suit as an admission* was directly contrary to the applicable decision of this Court. However, the action of the trial Court in refusing to permit the pleader to show that the allegations of his Bill had been judicially disproved and held contrary to fact, had the effect of making the same unimpeachable and constituted a denial of due process. Tot v. United States, 319 U. S. 463 (1943); Western

*Wigmore on Evidence (1904 Edition), Volume 2, Section 1065, P. 1243.

Atlantic R. Co. v. Henderson, 279 U. S. 639 (1929). In Saunders v. Shaw, 244 U. S. 317 (1917), Justice Holmes said, in reversing the State Court for refusal to permit cross-examination:

> "We cannot be sure the defendant's rights are protected without giving him a chance to put his evidence in."

When the trial Judge denied the Receiver the right to cross-examine and to put the evidence in the ruling constituted a departure from the accepted course of judicial procedure and also violated the constitutional requirement of due process.

Reasons Relating to Question 4.

Judge Simons points out that defendant gave "concededly false representations" to the Receiver and "concededly untrue evidence" in the trial below (R. 1371). This fact was discovered after the conclusion of the trial. Under these circumstances, it would seem clear that where the sole witness has given false testimony on material facts and the case is one in which the plaintiff is entitled to a jury, the case should have been remanded for re-examination of the issues at common law before the jury, and the Court did not have the right to take this fact issue from the jury. As the Opinion of Judge Simons states:

> "A jury should be permitted to appraise the accuracy of his memory and the credibility of his evidence, bearing upon the vital issues of the case in the light of the newly discovered facts."

We submit that this Court should exercise its supervisory powers to insure to plaintiff the verdict of a *jury* based on the truth and not on false evidence.

Reasons Relating to Question 5.

The assertion of a defense based on knowing participation with the Bank in concededly *ultra vires* acts "contravenes a general policy to protect the institution of banking" therefrom. D'Oench, Duhme & Co., Inc., v. F. D. I. C., 315 U. S. 447 (1942), at p. 458. In Dietrick v. Greaney, 309 U. S. 190 (1940), Mr. Justice Stone, in holding that the Bank Receiver could recover on a note given in substitution for shares of stock as a means of avoiding the consequences of violation of a statute, said (p. 196):

> "It is the evil tendency of the prohibited acts at which the statute is aimed, and its aid, in condemnation of them and in preventing the consequences which the act was designed to prevent, may be invoked by the Receiver representing the creditors for whose benefit the statute was enacted."

The Court of Appeals apparently recognized that if Tway had knowledge of the *ultra vires* character of the act and participated with the Bank, he ought not be permitted to recover, but said that the question of knowledge was a jury issue (R. 1367-8). However, the Court was mistaken in its apparent belief that the trial Court had submitted this issue to the jury. The trial

judge instructed the jury that the issue was "immaterial" (R. 1216).

The issue is material and involves an important question of Federal law pertaining to the protection of depositors and creditors of national banks and that this Court should review the decision, in order to correct the error below, in accordance with the applicable decisions of this Court.

Reasons Relating to Question 6.

We have previously pointed out that the ultimate loss of value of Banco stock was due to the independent acts of the corporation after defendant became a stockholder thereof. This loss was not due to any misrepresentations of the Bank. It was a loss for which this Court said, in Anderson v. Abbott, *supra, "The stockholders of Banco cannot escape responsibility."* However, the decision below permits Tway to avoid all responsibility for the acts of the corporation of which he was a stockholder which occurred long after the alleged misrepresentations. Assuming that misrepresentations were made concerning the value of the National Bank of Kentucky, the damages due to such misrepresentations should have been determined by way of counterclaim and applied in reduction of the liability of Tway on his note.

Tway borrowed $50,000.00 from the Bank. That money was credited to his account and was withdrawn from the Bank's assets by Tway's check and paid over to BancoKentucky Company. The Bank's assets were

thereby depleted. The Receiver should recover this money less any damage due to the Bank's misrepresentations. The gist of the so-called defense is that Tway was misled with respect to the purchase of the stock. Although designated a defense, it was in fact a counterclaim. The rules of civil procedure cover the situation. Rule 8(c) provides:

> "When a party has mistakenly designated a defense as a counterclaim or a counterclaim as a defense, the Court on terms, if justice so requires, shall treat the pleading as if there had been a proper designation."

An important question of Federal procedure is thus presented. Should the Court have carried out the mandatory provisions of the Rule? It was conceded that if Tway had made an affirmative claim, he could not recover the full value of the stock, but his recovery would be limited to the damages by reason of the vice which he claims existed at the time of its purchase. The lower Court, by failing to apply the rule permitted Tway to shift to the depositors of the National Bank of Kentucky the loss which resulted from the acts of the officers of Banco—acts which occurred long after his purchase. It is submitted that this calls for the exercise of this Court's supervisory jurisdiction.

CONCLUSION.

Petitioner has been denied the very essence of a fair trial. The opinion written by Judge Simons clearly elucidates a number of prejudicial errors which occurred in the trial. The opinion of Judge McAllister is limited to the sole question of the newly discovered evidence. No answer or comment is made with respect to any of the other vital and serious errors of the trial Court set forth by Judge Simons and elaborated herein. We respectfully submit that the petition for writ of certiorari should be granted.

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